Supreme Court, U.S.
FILED
JAN 9 1980
MICHAEL RODAK, JR., CLERK

No. 79-749

In the Supreme Court of the United States

OCTOBER TERM, 1979

CARLOS AND EMMA BLANCO, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

WADE H. MCCREE, JR.
Solicitor General
Department of Justice
Washington, D.C. 20530

In the Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-749

CARLOS AND EMMA BLANCO, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

Petitioner[1] seeks review of the decision below in this federal income tax case upholding the Commissioner of Internal Revenue's determination that a $65,200 distribution from his controlled corporation was a dividend taxable at ordinary income rates.

The pertinent facts are as follows: On July 31, 1970, petitioner surrendered to Carlos Blanco, Inc., a corporation 99% of the stock of which was owned by him and his wife, 2,281 shares of that company's common stock

---

[1] "Petitioner" refers to Carlos Blanco. Emma Blanco is a party solely because of having filed a joint income tax return for the year at issue.

in return for property[2] and in satisfaction of various debts owed by petitioner.[3] The total value of the property distributed and other benefits provided by the corporation to petitioner was $65,200 (Pet. App. A-1 to A-2).

Petitioner and his accountant testified that the purpose of this transaction was to distribute corporate assets to petitioner because some of the assets were already in petitioner's name and some corporate assets served no corporate purpose except as investments. Petitioners transferred some of his stock back to the corporation because he lacked the necessary cash to make the purchase. After completion of the transaction, petitioner's accountant learned that the distribution of property and other consideration from the corporation to petitioner were taxable to him as a dividend because the stock redemption had no significant effect upon Blanco's proportionate stock interest in the corporation. At the accountant's recommendation, petitioner gave the corporation a $65,200 note, bearing 5 1/2% interest, and the corporation returned the previously redeemed corporate shares to petitioner (Pet. App. A-2 to A-3).

---

[2]Petitioner received Citizens Bank stock worth $36,150, which had been purchased with company funds but held in his name; and the corporation's interest in Los Amadores, valued at $3,000; the corporation's stock interest in Pan American Savings & Loan, valued at $1,900, and the corporations interest in a joint venture, valued at $17,318 (Dep. 8-9, 11, 13, 21).

[3]The corporation satisfied the following obligations owed to it by petitioner: $1,148.19 owed on the Cleaning Center joint venture; interest of $562.14 and $292.05 owed to the First National Bank of Portales and the Southwest Bank of Amarillo, respectively; payments of $3,783.64 and $12.50 on a loan from Fernandez to petitioner; $40.40, representing Fed-Mart dividends payable to the corporation but cashed by petitioner, and $998.03, representing the balance due on amounts borrowed from the corporation by petitioner (Dep. 10, 11, 19-22).

The Court of Claims held that the second transaction was "an attempt by the taxpayer to reopen a completed transaction for a perceived tax advantage" (Pet. App. A-9) and did not alter the dividend treatment of the first transaction. Although petitioner's accountant testified that the purpose of this second transaction was to reverse the earlier transaction,[4] the Court of Claims correctly noted (Pet. App. A-6) that "the second transaction did not restore the parties to the *status quo ante*." In fact, Blanco was placed in a more favorable position after the second transaction because he obtained individual ownership of the assets which the corporation had previously owned. The court further ruled that petitioner was not entitled to deduct payments made to the corporation, where he voluntarily assumed the legal obligation represented by the $65,000 promissory note, in order to reduce his own tax liability (Pet. App. A-7 to A-8).[5]

The Court of Claims correctly held that petitioner's transfer of a note of his corporation did not mitigate the dividend consequences of the initial stock redemption. There is no question that the first transaction fully reflected the intentions of the parties: the transfer of corporate assets to petitioner and the use of corporate funds to satisfy petitioner's individual obligations (Pet.

---

[4]The accountant stated that a return of assets was not considered because a bonding company would not accept the corporation's interest in the joint venture as a corporate asset for bonding purposes, but would accept petitioner's individual promissory note (Pet. App. A-3).

[5]Petitioner does not challenge this aspect of the decision below that his subsequent voluntary determination to pay an amount equal to the redemptive distribution to the corporation would not support a deduction because such payments would be capital contributions. Cf. *Crellin's Estate* v. *Commissioner*, 203 F. 2d 812 (9th Cir.), cert. denied, 346 U.S. 873 (1953); *United States* v. *Simon*, 281 F. 2d 520 (6th Cir. 1960); *Pahl* v. *Commissioner*, 67 T.C. 286, 290 (1976).

App. A-2 to A-3; Dep. 25.) In these circumstances, where the redemption of petitioner's stock had "no significant effect upon [his] ownership interest in the corporation" (Pet. App. A-3), it was essentially equivalent to a dividend within the meaning of Sections 301, 302 and 316 of the Internal Revenue Code of 1954 (26 U.S.C.). See *United States* v. *Davis*, 397 U.S. 301 (1970).

The Court of Claims properly rejected petitioner's subsequent attempt to "reopen and alter a transaction that was valid and complete for business purposes in order to obtain more favorable tax treatment" (Pet. App. A-8) by substituting his promissory note for the stock interest which actually served as the consideration. As this Court observed in *Commissioner* v. *Nat. Alfalfa Dehydrating*, 417 U.S. 134, 149 (1974):

> [W]hile a taxpayer is free to organize his affairs as he chooses, nevertheless, once having done so, he must accept the tax consequences of his choice, whether contemplated or not, *Higgins* v. *Smith*, 308 U.S. 473, 477 (1940); *Old Mission Portland Cement Co.* v. *Helvering*, 293 U.S. 289, 293 (1934); *Gregory* v. *Helvering*, 293 U.S. 465, 469 (1935), and may not enjoy the benefit of some other route he might have chosen to follow but did not. "To make the taxability of the transaction depend upon the determination whether there existed an alternative form which the statute did not tax would create burden and uncertainty." *Founders General Corp.* v. *Hoey*, 300 U.S. 268, 275 (1937); *Television Industries, Inc.* v. *Commissioner*, 284 F. 2d 322, 325 (CA2 1960); *Interlochen Co.* v. *Commissioner*, 232 F. 2d 873, 877 (CA4 1956). See *Gray* v. *Powell*, 314 U.S. 402, 414 (1941).

Indeed, this Court has never permitted a taxpayer to recharacterize a transaction merely because unfortunate tax consequences were discovered after the event.[6] Cf. *United States* v. *Lewis*, 340 U.S. 590, 591 (1951).

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.
Solicitor General

JANUARY 1980

---

[6]As the Court of Claims noted (Pet. App. A-7 n.3) *Meyer's Estate* v. *Commissioner*, 200 F. 2d 592 (5th Cir. 1962), upon which petitioner relies (Pet. 10), is distinguishable. That case involved a taxpayer who was permitted to withdraw unilaterally an election because it had been based upon a misapprehension as to the extent of surplus possessed by a corporation. The taxpayer was aware of the law, but made a decision "upon a computational error" (Pet. App. A-7). Here, on the other hand, petitioner failed to undo his first agreement with the corporation. Moreover, he does not suggest the first transaction which he thereafter attempted to modify was executed upon a misapprehension of fact.